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IN THE

Supreme Court of the United States

October Term, 1966

No. 1354

READING COMPANY,

Petitioner

v.

FRANCIS SHUNK BROWN, 3RD, Trustee of the Estate of I. J. KNIGHT REALTY CORP., Bankrupt,

Respondent,

and

UNITED STATES OF AMERICA,

Respondent.

BRIEF OF RESPONDENT FRANCIS SHUNK BROWN, 3RD, TRUSTEE OF THE ESTATE OF I. J. KNIGHT REALTY CORP., BANKRUPT, IN OPPOSITION TO PETITION FOR CERTIORARI.

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OPINIONS BELOW.

The opinion of the Referee in Bankruptcy is not reported, but is printed in the record at 22a et seq. The opinion of the District Court, with its appendix (35a) is reported at 242 F. Supp. 337. The majority and dissenting opinions of the Court of Appeals for the Third Circuit are printed in petitioner's Appendix C, pp. 11-22, and have now been reported at 370 F. 2d 624.

JURISDICTION.

The judgment of the Court of Appeals was entered on January 6, 1967. An order of the Court of Appeals denying petitioner's petition for rehearing was entered on February 13, 1967. Petitioner seeks to invoke the jurisdiction of this court under 62 Stat. 928, c. 646, 28 U. S. C. § 1254(1).

QUESTION PRESENTED.

Is an unliquidated negligence claim against a receiver which arises during a Chapter XI proceeding entitled to a first priority as an "actual and necessary cost [or expense of administration]" as that term is used in Sections 62a(1) and 64a(1) of the Bankruptcy Act?

STATUTES INVOLVED.

The pertinent statutory provisions are Sections 62a(1), 63a(7), 64a and 77n of the Bankruptcy Act; 11 U. S. C. § 102(a)(1), § 103(a)(7), § 104(a) and § 205(n) respectively. All of said sections except § 77n (and § 64a, only a portion of which was printed) have been printed at pages 9 and 10 of the petition. Sections 64a and 77n are printed in full in respondent's Appendix, *infra,* at pp. A1 to A3.

This respondent contends that there are no constitutional issues present here, and hence, no constitutional provisions involved.

STATEMENT OF THE CASE.

On November 16, 1962, I. J. Knight Realty Corporation filed a petition in the District Court for the Eastern District of Pennsylvania for an arrangement under Chapter XI of the Bankruptcy Act. Francis Shunk Brown, 3rd, Esquire was appointed receiver to operate the business of the debtor, whose principal asset was an 8-story industrial structure known as the Fretz Building, located at 10th and Diamond Streets in Philadelphia.

On January 1, 1963, a fire of unusual intensity, fanned by winds of exceptionally high velocity completely destroyed the Fretz Building. It was a twelve-alarm fire, and the biggest in the history of Philadelphia (6a). The fire also damaged or destroyed adjoining property, including property of the Reading Company.

Thereafter, the Reading Company filed a claim in the bankruptcy proceeding styled a claim for "administration expenses due to the negligence of the Receiver in operation of the business of the debtor." On May 14, 1963, the corporation was adjudicated a bankrupt pursuant to a voluntary consent to adjudication. The receiver was elected trustee, and as such filed a petition to expunge the Reading Company's claim as not being a "cost of expense of administration" as that term is used in the Bankruptcy Act. The trustee and the Reading Company submitted the issues presented by the trustee's petition on the basis of a case-stated (20a).

Referee Thomas J. Curtin granted the prayer of the trustee's petition in an opinion and order which holds that the Reading Company's claim does not qualify as a cost or expense of administration under Section 64a(1) and is not provable as an unsecured claim under Section 63 of the Act (22a). In an opinion and order dated June 9, 1965,

the Honorable Francis L. Van Dusen of the District Court for the Eastern District of Pennsylvania, affirmed Referee Curtin's order (35a). Subsequently a majority of the United States Court of Appeals for the Third Circuit, per Judge Kalodner, affirmed Judge Van Dusen's order (Petitioner's Appendix C, p. 11; 370 F. 2d 624).

ARGUMENT.

This is not a case in which the Court below is establishing a general rule foreclosing large groups of victims from recovery of tort damages. This is a case in which the priorities established by Congress in the Bankruptcy Act have been applied. Priorities alone are involved here, and not substantive rights. The struggle is between the qualified creditors of the bankrupt on the one hand, and on the other, the railroad company, and, presumably, the companies which took the risk of insuring adjacent property owners from loss by fire. These parties have a remedy under 28 U. S. C. § 959, in a plenary action. Their claims are not discharged in the bankruptcy proceeding. As the court below intimated, the receiver appointed to operate a business under Chapter XI, like any other prudent business man, takes out public liability insurance.

Surely at other times and places torts have been committed by bankrupts to or against property contiguous to theirs, or to persons in the vicinity of or on a bankrupt's property, or by vehicles belonging to bankrupts. No case, however, has been found in which a contention similar to that of the present petitioner has been made. The reason for the absence of cases may be that the liability insurance proceeds were adequate to pay losses incurred. In the present situation the fire was of woefully unique proportions, and no reasonably foreseeable insurance coverage could possibly have been adequate or even carried.

Although Congress has on a number of occasions considered and amended the Bankruptcy Act, it has never chosen to amend Section 63a(7), the only section dealing with provable tort claims other than Section 77n. The latter was added by amendment to deal with injuries and death of railroad employees, which first were recognized by Congress in an earlier amendment in 1933 (38a, footnote 2). Under the provisions of Section 63a(7), tort claims to be

provable must have been instituted "prior to" and be "pending at the time of the filing of the petition in bankruptcy . . ."

A. This Case Establishes No New or Unusual Principle.

This case is unusual because the holocaust wiped out the bankrupt's business, which in turn resulted in the creation of a fund. Were it not for such fund, this litigation would never have been instituted. The existence of a fund doesn't authorize the courts to alter statutory priorities governing distribution as established by Congress. Where Congress, by statute, has provided how a fund is to be distributed (See Section 64a, Appendix p. A1), courts should not, under the guise of applying equitable principles, set aside, ignore or modify the statutory mandates. Under the provisions of Section 63a, negligence claims cannot be proved unless they are instituted prior to, and are pending at the time of the petition in bankruptcy. Contrary to such a provision, petitioner is asking this Court not only to permit such a claim which arose subsequent to the filing of the petition to be proved, but also to be granted priority ahead of all other claims, of whatsoever nature, general or preferred.

B. The Decision Below Was Correct.

Congress, in enacting and amending the bankruptcy laws, has spoken twice on the proof and allowance of tort claims (Sections 63a(7) and 77n). In bankruptcy, tort claims to be provable, must have been pending when the petition was filed. Even when tort claims are properly pending and therefore provable, they are granted no priority (p. A1; petition, p. 10). In railroad receiverships, claims for deceased or injured employees are paid as operating expenses (Section 77n, p. A3). The Court below concluded (Appendix C to petition, p. 16) that this congressional design disclosed an intention not to include any other tort claims arising during the receivership, and

specifically, not to permit them a priority status under Section 64a(1) as a cost or expense of administration. In a case discussing Section 67(c) in its relationship to Section 64a(1) and (2), this Court, in *Goggin v. California Labor Division*, 336 U. S. 118 (1949), at p. 127, alluded to the narrowness of the priority of administrative expenses and wage claims.

As this Court said in *U. S. v. Embassy Restaurant, Inc.*, 359 U. S. 29, 31 (1959), ". . . [I]f one claimant is to be preferred over others, the purpose should be clear from the statute.' At page 35, this Court said "Under the Bankruptcy Act . . . not all claims 'justly due' have priority. They must be within a class such as 'wages . . . due to workmen.' The claims here are not. If this class is to be so enlarged, it must be done by the Congress."

C. The Reasons Advanced by the Petitioner for the Grant of Certiorari Are Without Merit.

The reasons advanced by the petitioner in support of its petition are dealt with in the following correspondingly numbered paragraphs:

1. *There Is No Constitutional Issue.*

There has been no denial of due process here, and the cases cited to the contrary are not germane. The object of the bankruptcy statutes is the equitable distribution of the debtor's assets among his creditors. Congress, in determining what such an equitable distribution demands, is free to establish standards of proof and measures of allowance regardless of the claimant's ability to maintain an action in a court or the measure of his recovery in such an action if maintainable. *Kuehner v. Irving Trust Co.*, 299 U. S. 445, 451 (1937). The size of the holocaust may lend the present case a certain dramatic impact, but this circustance does not call for the invocation of constitutional rights.

2. *The Decision Below Is Not at Variance With § 959 of the Judicial Code.*

The assertion that Section 959 of the Judicial Code (28 U. S. C. § 959) is nullified is without merit. This Section is an administrative one, lumped together with various others having to do with the duties and responsibilities of court clerks, expenses of running their offices, etc. The fact that it codifies the right to sue a trustee does not automatically carry with it the further requirement that any judgment so recovered be collectible. Many judgment creditors are unable to collect their judgments, but it has never yet been held that this circumstance rendered inoperative the statute under which they brought suit. Petitioner has been deprived of no remedy or redress. He has merely been denied the right to participate in the distribution of the assets in the bankrupt estate. His claim has not been discharged by bankruptcy. He can still pursue the debtor after the administration of the estate has been completed.

3. *The Decision Below Will Not Affect Prudent Administration by Receivers.*

The argument that receivers will fear to carry liability insurance because of the opinion below is without merit. Under no circumstances would anyone, whether he were the receiver, or the owner of a going concern, who was operating a building like the one involved here, take out liability insurance sufficient to cover the losses which ultimately resulted in this case. The court below recognized this and intimated correctly that this was a liability which could not reasonably be anticipated. Of course reasonable insurance precautions will continue to be taken in the future as they have in the past, under the guidance of the Bankruptcy Court, if necessary.

As in the past, the insurance taken out by the receiver will be sufficient to protect against the cornice falling off or the faulty sidewalk. The everyday practices of receivers in this respect, their rights and liabilities, and those of the

people with whom they deal, will in no wise be affected by the outcome of this case; and it is safe to say that any rule which might be fashioned by this Court at the behest of the petitioner will have applicability to this case and this case alone.

4. *There Is No Conflict With Prior Decisions of This Court.*

(a) For petitioner to say that the Bankruptcy Act should be construed in accordance with equity jurisprudence is to say that this Court should substitute petitioner's notion of equity for that which Congress has enacted. If the property damage claimants were to be granted the priority they seek, all other claims, priority and otherwise, would be extinguished many times over, and their claims would be discharged. The cases cited by petitioner do not support its contention.

(b) In support of petitioner's contention that this Court has held that claims for receiver's torts are priority claims, petitioner cites the old railroad cases. At the risk of repetition, it must again be said that these illustrate that when Congress wishes to favor a type of tort claimant, it knows how to do so, and will not leave the matter to the hazards of development through case law.

Other than the torts dealt with in Section 63a (Petition, p. 10), only one class of tort claimant has had the treatment accorded it which the petitioner is urging here, and that is the class described in Section 77n (p. A3), namely injured railroad employees, and personal representatives of deceased railroad employees. If Congress had desired to extend this priority to other tort claimants, it would certainly have done so.

5. *There Is No Conflict of Decision Between Circuits.*

As the District Court pointed out in its opinion (42a), there are no cases which have directly considered the pres-

ent issue. The reasons for this have already been alluded to. The present factual situation is unique and likely to remain so. Therefore, contrary to petitioner's assertion, its case is not in conflict with the Second Circuit case cited, *Vass v. Conron Bros.*, 59 F. 2d 969 (2d Cir. 1932). That case simply held that the bankruptcy court was the proper forum to determine a lessee's claim for damages against the trustee arising from the trustee's operation of the premises. Both the referee and the district judge found the portions of that opinion relied upon by petitioner to be dictum (26a, 47a). Apart from the fact that *In re Progress Lektro Shave Corp.*, 35 F. Supp. 915 (D. Conn. 1940) is not a Court of Appeals case, it is clearly distinguishable from the present one, and therefore creates no conflict. As the district judge pointed out (46a), that case involved a trustee selling for the benefit of the bankrupt estate an article covered by the claimant's patent. To have denied the claimant recovery would have been to deny him the right to his own property and have permitted unjust enrichment to the bankrupt estate. There is no such element in the case at bar.

Not only is there no conflict among circuits, but rulings in analogous cases, even though not strictly on point, disclose that generally, where Section 64a has been considered, the courts have refrained from using it as a catch-all for post-bankruptcy items at the behest of aggrieved claimants. An example of such a case is *In re Connecticut Motor Lines, Inc.*, 336 F. 2d 96 (3d Cir. 1964), discussed and quoted at length by the Referee (27a et seq.), the District Court (40a), and the Court below (petition, pp. 14, 15). Briefly stated, there is no holding among the Courts of Appeals which would lend color to a contrary argument.

6. *There Is No Departure From the Accepted Principles of Statutory Interpretation or of Equity Jurisprudence, Nor Variance From the Views of the Text Writers.*

Statutory interpretation has been dealt with above under other headings. The Referee and the Courts below have construed the Bankruptcy Act consistently with the intention of Congress. Petitioner has cited texts having to do with equity receiverships, but these are not authority for bankruptcy administration, and the bankruptcy acts have never been regarded as a codification of existing equity practice. The most that can be gleaned from the cited works of Collier on the present problem is that costs and expenses will be carefully examined to see that they have been for the purpose of aiding the administration of the estate or enhancing its value before they will be recognized as deserving to be included within the priority here discussed.

CONCLUSION.

For the reasons stated it is respectfully submitted that this petition for a writ of certiorari should be denied.

Respectfully submitted,

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June 2, 1967.

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